No. 15350

IN THE

United States Court of Appeals For the Ninth Circuit

William B. Cammarano and Louise Cammarano, His Wife, *Appellants*

v.

United States of America, *Appellee*

On Appeal from the Judgment of the United States District Court for the Western District of Washington

BRIEF FOR THE APPELLEE

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INDEX

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BRIEF FOR THE APPELLEE

OPINION BELOW

The oral decision of the District Court (R. 27-30) is not officially reported.

JURISDICTION

This appeal involves federal income taxes for the year 1948. The taxes in dispute, $153.58, were paid on October 16, 1951. (R. 20-21.) A claim for refund was filed on December 29, 1951. (R. 11-12, 21.) No

action having been taken on the claim (R. 21) within the time provided in Section 3772 of the Internal Revenue Code of 1939, and on March 15, 1955, taxpayers brought an action in the United States District Court for the Western District of Washington for recovery of the taxes paid. (R. 3-12.) Jurisdiction was conferred on the District Court by 28 U.S.C., Section 1346. The oral decision of the District Court was entered on March 28, 1956. (R. 27-30, 127.) The findings of fact, conclusions of law and judgment of the District Court were entered on July 30, 1956. (R. 43-50, 127.) On September 6, 1956, taxpayers filed a notice of appeal. (R. 51.) The jurisdiction of this Court is invoked under 28 U.S.C., Section 1291.

QUESTION PRESENTED

Whether the District Court was correct in disallowing a deduction to taxpayers under Section 23(a)(1)(A) of the Internal Revenue Code of 1939, for the amounts paid by taxpayers to a special fund to finance a publicity program to influence the voters of the State of Washington to vote to defeat an Initiative which would have prohibited the retail sale of beer and wine by any person other than the State of Washington.

STATUTE AND REGULATIONS INVOLVED

Internal Revenue Code of 1939:

Sec. 23. Deductions From Gross Income.

In computing net income there shall be allowed as deductions:

(a) [As amended by Section 121(a) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Expenses.*—

(1) *Trade or Business Expenses.*—

(A) *In General.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, * * *.

* * * * *

(26 U.S.C. 1952 ed., Sec. 23.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

Sec. 29.23(o)-1. *Contributions or Gifts by Individuals.*— * * *

* * * * *

Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income.

* * * * *

STATEMENT

The relevant facts as found by the District Court (R. 44-47) may be summarized as follows:

Taxpayers were husband and wife and filed a joint income tax return for the year 1948. They owned a one-quarter interest in a partnership carrying on wholesale distribution of beer under the trade name "Cammarano Brothers" in Tacoma, Washington. (R. 44-45.)

During 1948, the partnership paid $3,545.15 to the Washington Beer Wholesalers Association, Inc., Trust Fund, taxpayers' proportionate share of such payment being $886.29. The trust fund had been established on December 17, 1947, by the association of

which the partnership was a member, to help finance a state-wide publicity program on the part of wholesale beer and wine dealers. (R. 45.)

This publicity program urged the defeat of Initiative to the Legislature No. 13, which was submitted to the people of Washington in accordance with the legislation provisions of the State Constitution at the general election on November 2, 1948. The Initiative would have placed the retail sale of wine and beer exclusively in state owned and operated stores. The ballot title of the Initiative was as follows (R. 45):

> An Act prohibiting the retail sale of beer and wine by any person other than the State of Washington, repealing all provisions of existing law pertaining to licensing of retail sale of beer and wine, revoking existing licenses and providing penalties.

The measure had previously been submitted to the state legislature. An officer of the Beer Wholesalers Association kept close track of its progress, and personally contacted many of the legislators and urged its defeat. The legislature did not act on the measure. (R. 45-46.)

With the measure going before the people, the wholesale and retail wine and beer dealers decided to undertake a vast publicity program aimed at the people who were to vote on the measure in November, 1948. It was decided that the program should be directed by a committee made up from the various groups and associations interested in defeat of the measure, and financed by contributions from those groups and associations and other interested parties. An Industry Advisory Committee was established to direct the program, in support of which it was furnished with $231,257.10. Of

that amount, $53,500 came from the Beer Wholesalers Association, which collected the money by assessing its members amounts based upon their volume of business. The collections were handled by the association through a trust fund, which was established as a separate entity to receive and disburse the assessments. The program was carried out by various types of advertising. None of this advertising had reference to the wares or members of the association as such. (R. 46.)

There was testimony to the effect that the Initiative, if passed, would have affected the wholesale business of Cammarano Brothers. However, the way in which the measure, aimed as it was at retail sales of wine and beer, would have affected the wholesale distribution of beer was not made clear. In any event, the measure was defeated. (R. 46.)

As early as September 3, 1937, the Commissioner ruled that the Beer Wholesalers Association was exempt from federal income tax. During the period of the publicity program the association continued its usual activities and collected its usual dues from its members, including Cammarano Brothers. (R. 47.)

The District Court found that the payment made to the trust fund by Cammarano Brothers was entirely for propaganda and aimed at the defeat of legislation, and therefore was not deductible under Section 23(a)(1)(A) of the Internal Revenue Code of 1939, as an "ordinary and necessary expense paid or incurred during the taxable year in carrying on" its business of the wholesale distribution of beer. (R. 47-48.)

SUMMARY OF ARGUMENT

The Internal Revenue Code of 1939 does not allow a deduction for all expenses paid or incurred by a business. Section 23(a)(1)(A) of the 1939 Code permits a deduction for "ordinary and necessary expenses" incurred "in carrying on any trade or business * * *." Section 29.23(o)-1 of Treasury Regulations 111, promulgated under the 1939 Code prohibits the deduction of "sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses * * *."

The regulation uniformly has been held to apply to Section 23(a)(1)(A) of the statute and to be a valid limitation upon what items may be deducted as "ordiary and necessary" expenses of "carrying on" a business. Furthermore, it is well recognized that the regulation is not limited only to expenses of lobbying before a legislature, for the regulation applies as well to publicity campaigns directed at voters who are to vote on a measure. Additionally, it is recognized that it is immaterial whether such lobbying, or the promotion or defeat of legislation, or propaganda, etc., is against "public policy" for the regulation applies to all attempts to influence the promotion or defeat of legislation.

Thus, in the present case, where taxpayers expended sums upon advertising, etc., to persuade the voters to defeat an Initiative, the sums were expended for the "defeat of legislation" and for "advertising other than trade advertising" within the meaning of the regulation, and a deduction for such amounts was properly denied by the District Court.

ARGUMENT

The District Court Was Correct in Holding That Amounts Expended to Influence Voters to Defeat an Initiative Which Would Have Prohibited the Retail Sale of Beer and Wine by Any Person Other Than the State of Washington Did Not Constitute an Ordinary and Necessary Expense Incurred in Carrying on Taxpayers' Business of the Wholesale Distribution of Beer Under Section 23(a)(1)(A) of the Internal Revenue Code of 1939 and Section 29.23(o)-1 of Treasury Regulations 111

This case concerns the applicability of Section 23 (a)(1)(A) of the Internal Revenue Code of 1939, *supra,* and of Section 29.23(o)-1 of Treasury Regulations 111, *supra,* promulgated under the 1939 Code.

During 1948, the partnership, Cammarano Brothers, in which taxpayers had a 25 per cent interest, paid \$3,545.15 to the Washington Beer Wholesalers Association, Inc., Trust Fund to help finance an extensive statewide publicity program to influence the voters of the State of Washington to defeat Initiative 13 at the general election on November 2, 1948. This Initiative would have placed the retail sale of wine and beer exclusively in state-owned and operated stores. An industry Advisory Committee was established to direct the program to defeat the Initiative, in support of which it was furnished with \$231,257.10. Of this amount, \$53,500 came from the Beer Wholesalers Association, which collected its share of the money by assessing its members amounts based upon their volume of business. The Industry Advisory Committee spent the money received by it primarily on advertising, and also for printing, public relations expenses, etc. (R. 21-23, 45-46, 79, 82-84, 103-107, 112-116, Exs. 7, B. E.)

Taxpayers seek to deduct their aliquot share of the amount which Cammarano Brothers paid to the Beer Wholesalers Association as an ordinary and neces-

sary business expense of the partnership under Section 23(a)(1)(A) of the 1939 Code. The District Court held (R. 47-48) that the payment "was entirely for propaganda" and was "aimed at the defeat of legislation", and accordingly was not deductible as an "ordinary and necessary" trade or business expense under Section 23(a)(1)(A).

The relevant portion of Section 23(a)(1)(A) is as follows:

> In computing net income there shall be allowed as deductions:
>
> (a) *Expenses.*—
>
> (1) *Trade or Business Expenses.*—
>
> (A) *In General.*—All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, * * *.
>
> * * * * *

The provisions of Section 29.23(o)-1 of Treasury Regulations 111, which control taxpayers' right to a deduction, are as follows:

> Sums of money expended for lobbying purposes, the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and contributions for campaign expenses, are not deductible from gross income.

The court decisions which have construed these provisions have uniformly held that sums of money spent for lobbying, for the promotion or defeat of legislation, for campaign purposes, etc., and which are similar to the payments made in the present case do not constitute the ordinary and necessary expenses of carry-

ing on a trade or business and, accordingly, are not deductible under Section 23(a)(1)(A). *Textiles Mills Corp.* v. *Commissioner,* 314 U.S. 326; *McDonald* v. *Commissioner,* 323 U.S. 57; *Sunset Scavenger Co.* v. *Commissioner,* 84 F. 2d 453 (C.A. 9th); *Old Mission P. Cement Co.* v. *Commissioner,* 69 F. 2d 676 (C.A. 9th); *Revere Racing Assn.* v. *Scanlon,* 232 F. 2d 816 (C.A. 1st); *American Hardware & Eq. Co.* v. *Commissioner,* 202 F. 2d 126 (C.A. 4th); certiorari denied, 346 U.S. 814; *Roberts Dairy Co.* v. *Commissioner,* 195 F. 2d 948 (C.A. 8th), certiorari denied, 344 U.S. 865; *Mays* v. *Bowers,* 201 F. 2d 401 (C.A. 4th), certiorari denied, 345 U.S. 969; *Davis* v. *Commissioner,* 26 T.C. 49; *McClintock-Trunkey Co.* v. *Commissioner,* 19 T.C. 297, reversed on another issue, 217 F. 2d 329 (C.A. 9th); *Wm. T. Stover Co.* v. *Commissioner,* 27 T.C. No. 48; *Bellingrath* v. *Commissioner,* 46 B.T.A. 89; *Cullen* v. *Commissioner,* 41 B.T.A. 1054; *Kyne* v. *Commissioner,* 35 B.T.A. 202; *Mosby Hotel Co.* v. *Commissioner,* decided October 22, 1954 (1954 P-H T.C. Memorandum Decisions, par. 54,288).

At the outset, taxpayers question (Br. 11-22) whether this prohibition contained in Section 29.23(o)-1 of the Regulations is applicable to Section 23(a)(1)(A) of the statute. Taxpayers attempt to make much of the fact that the predecessor of Section 29.23(o)-1 is entitled "Donations" and deals in large part with charitable contributions by individuals, whereas Section 23(a)(1)(A) is concerned with deductions for business expenses.

Such contentions, however, are conclusively answered by the following decisions, which hold, in response to direct attacks on the applicability of the prohibition in the Regulations to the business expense

provision of the statute, that it is applicable. *Textile Mills Corp.* v. *Commissioner, supra; Sunset Scavenger Co.* v. *Commissioner, supra; American Hardware & Eq. Co.* v. *Commissioner, supra; Revere Racing Assn.* v. *Scanlon, supra; McClintock-Trunkey Co.* v. *Commissioner, supra; Bellingrath* v. *Commissioner, supra.* As the Supreme Court has stated in *Textile Mills Corp.* v. *Commissioner, supra* (pp. 337-338):

> If this is a valid and applicable regulation, the sums in question were not deductible as "ordinary and necessary expenses" under § 23 (a), since they clearly run afoul of the prohibition in the last sentence of the regulation.
>
> Plainly, the regulation was applicable. The ban against deductions of amounts spent for "lobbying" as "ordinary and necessary" expenses of a corporation derived from a Treasury Decision in 1915. T.D. 2137, 17 Treas. Dec., Int. Rev., pp. 48, 57-58. That prohibition was carried into Art. 143 of Treasury Regulations 33 (Revised, 1918) under the heading of "Expenses" in the section on "Deductions." Beginning in 1921 the regulation was entitled "Donations." (Art. 562, Treasury Regulations 45.) And in the regulations here in question Art. 262 appeared under § 23 (n), which covered "Charitable and other contributions" by individuals. It assumed that form and content in 1921 and appeared since then without change in all successive regulations. Sec. 23 (n) and § 23 (a) both deal with deductions; and a "donation" by a corporation though not deductible under the former might be under the latter. Art. 262 purports to specify when a certain type of expenditure or donation by a corporation may or may not be deducted as an "ordinary and necessary" expense. The argument that it was not

applicable because it was not specifically incorporated under § 23 (a) is frivolous.[1]

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[1] From almost the inception of the present income tax law, the Treasury has continuously and unambigously ruled that amounts spent for "lobbying" and for "the promotion or defeat of legislation" are not ordinary and necessary business expenses. The first published ruling appeared in T.D. 2137, 17 Treasury Decisions 48, 57-58 (1915), which declared that "Sums of money expended for lobbying purposes and contributions for campaign expenses are held not to be an ordinary and necessary expense in the *operation* and *maintenance* of the business of a corporation, and are, therefore, not deductible from gross income in arriving at the net income upon which the income tax is computed." (Emphasis supplied.) This determination, elaborated to refer expressly to expenditures for "the promotion or defeat of legislation," was incorporated as Article 143 of Treasury Regulations 33 (1918 ed.), wherein it was indicated that this was an interpretation of the phrase "ordinary and necessary." The regulation assumed its present form in Article 562 of Treasury Regulations 45 (1919 ed.), promulgated under the Revenue Act of 1918, and has since appeared without change, in all successive Regulations. See Article 562 of Treasury Regulations 45 (1920 ed.), 62, 65 and 69, promulgated under the Revenue Acts of 1918, 1921, 1924, and 1926, Article 262 of Treasury Regulations 74 and 77 (1929 and 1937 eds.), promulgated under the Revenue Acts of 1928 and 1932, Article 23(o)-2 of Treasury Regulations 86, promulgated under the Revenue Act of 1934, Article 23(q)-1 of Treasury Regulations 94, promulgated under the Revenue Act of 1936, Article 23(o)-1 of Treasury Regulations 101, promulgated under the Revenue Act of 1938, Sections 19.23(o)-1, 29.23(o)-1 and 39.23(o)-1 of Treasury Regulations 103, 111 and 118, respectively, promulgated under the Internal Revenue Code of 1939, and Section 1.162-15 of the proposed Income Tax Regulations under the Internal Revenue Code of 1954.

As pointed out, *supra,* both T.D. 2137, and Article 143 of Treasury Regulations 33 (1918 ed.), were an interpretation of the phrase "ordinary and necessary", and both incorporated the prohibition under provisions labelled "Lobbying Expenses". Beginning with Treasury Regulations 45 (1919 ed.), this provision was incorporated for reasons of convenience in the article relating to corporate deductions, entitled "Donations". Prior to 1928,

Taxpayers contend, in effect (Br. 45-47), that the Supreme Court in *Textile Mills, supra,* relied upon the fact that the trade or business expense provision "was the only possible section under which the Regulation relating to corporations could fall" in holding that the Regulations were applicable to Section 23(a)(1)(A); that the statute subsequently was amended to permit corporations to deduct for donations; and that the retention of the prohibition in the provision of the regulations relating to corporate donations showed an intent that the Regulations should not be applicable in the future to Section 23(a)(1)(A) of the statute. Such a contention is not well founded. This, plainly, is only a repetition of the argument made in *Textile Mills.* As previously pointed out (fn. 1, *supra*), prior

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there were separate provisions in the Revenue Acts dealing with expenses allowable to individuals and expenses allowable to corporations, although the provisions were identical. Moreover, these early Revenue Acts provided for deductions to individuals for charitable contributions, but made no similar provision for corporations. However, it was recognized that such donations might, under some circumstances, qualify as "ordinary and necessary" business expenses of a corporation. Accordingly, there appeared in the Regulations, under the statutory provisions relating to corporate donations, an article indicating when such donations were deductible as expenses. Since lobbying and other similar expenses were thought to be loosely related to donations, the provisions dealing therewith were likewise incorporated in the same article. It should be noted that this prohibition was not included during these many years in the articles of the Regulations dealing with charitable donations by individuals, although the articles dealing with individuals did refer to the articles relating to corporate donations. Thus, it is clear that the Regulations spelled out when such expenditures might or might not be deductible as "ordinary and necessary" business expenses.

In 1928, the structure of the revenue statute was simplified, and expense deductions for corporations and individuals were incorporated in a single section, namely, Section 23(a). Under the

to the decision in *Textile Mills* the prohibition could have been placed in the section of the Regulations dealing with trade or business expenses, but the Supreme Court held that an argument based upon the Commissioner's failure to have made such a placement was frivolous. There is no indication that the continued retention of the prohibition in the section of the Regulations relating to corporate donations after Section 23 (q) of the statute was enacted was for reasons other than convenience. The failure to repeat the prohibition in every subsection of the Regulations under which a deduction might be claimed is of no more weight here than it was in *Textile Mills. American Hardware & Eq. Co.* v. *Commissioner, supra,* pp. 129-130.

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reorganized structure, charitable contributions by individuals were dealth with in Section 23(n). However, no similar provision for corporations was enacted until Section 102(c) of the Revenue Act of 1935, c. 829, 49 Stat. 1014, which added Section 23(r) to the Revenue Act of 1934, c. 277, 48 Stat. 680 (later changed to Section 23(q) of the Revenue Act of 1936, c. 690, 49 Stat. 1648). For functional reasons, it was considered to be more desirable to continue thereafter the prohibition against these deductions in the regulatory provisions dealing with corporate donations. Although the provision relating to the deductibility of donations by individuals had existed in the Regulations for many years a similar prohibition was not included in the provisions of the Regulations dealing with individuals until 1939, and then by Article 23(o)-1 of Treasury Regulations 101. Thus, it is clear from the origin of these provisions, as well as from their content, that they are concerned with the question whether expenditures for lobbying purposes, the promotion or defeat of legislation, etc, are deductible as ''ordinary and necessary'' business expenses. This is further shown by the fact that in the proposed Income Tax Regulations under the 1954 Code this prohibition is contained in Section 1.162-15, which is placed under Section 162, dealing with trade or business expenses, rather than under Section 170, dealing with charitable and other contributions by individuals and corporations.

Taxpayers' contention (Br. 23-34, 37-42), that Section 29.23(o)-1 is invalid to the extent that it seeks to limit the deduction of certain expenditures as "ordinary and necessary" expenses of a trade or business under Section 23(a)(1)(A) of the 1939 Code, likewise lacks substance. This provision of the regulation has authoritatively been held valid. The general principle that repeated congressional reenactment of the statutory provision to which a regulation pertains, here Section 23(a)(1)(A) of the 1939 Code, gives to the Regulations the force of law (*Helvering* v. *Winmill,* 305 U.S. 79, 83; *Commissioner* v. *Flowers,* 326 U.S. 465, 469; *Boehm* v. *Commissioner,* 326 U.S. 287, 291-292), has been repeatedly applied to this particular provision in answer to direct challenges as to its validity (*Textile Mills Corp.* v. *Commissioner, supra,* pp. 338-339; *Sunset Scavenger Co.* v. *Commissioner, supra,* p. 456; *Roberts Dairy Co.* v. *Commissioner, supra,* p. 950; *American Hardware & Eq. Co.* v. *Commissioner, supra,* pp. 129-130; see *Commissioner* v. *Heininger,* 320 U.S. 467, 470; *Lilly* v. *Commissioner,* 343 U.S. 90, 95). The Supreme Court has stated in *Textile Mills Corp.* v. *Commissioner, supra* (pp. 338-339):

> Petitioner's argument that the regulation is invalid likewise lacks substance. The words "ordinary and necessary" are not so clear and unambiguous in their meaning and application as to leave no room for an interpretative regulation. The numerous cases which have come to this Court on that issue bear witness to that. *Welch* v. *Helvering,* 290 U.S. 111; *Deputy* v. *du Pont* 308 U.S. 488, and cases cited. Nor has the administrative agency usurped the legislative function by carving out this special group of expenses and making them non-deductible. We fail to find

any indication that such a course contravened any Congressional policy. Contracts to spread such insidious influences through legislative halls have long been condemned. *Trist* v. *Child,* 21 Wall. 441; *Hazelton* v. *Sheckells,* 202 U.S. 71. Whether the precise arrangement here in question would violate the rule of those cases is not material. The point is that the general policy indicated by those cases need not be disregarded by the rule-making authority in its segregation of non-deductible expenses. There is no reason why, in absence of clear Congressional action to the contrary, the rule-making authority cannot employ that general policy in drawing a line between legitimate business expenses and those arising from that family of contracts to which the law has given no sanction. The exclusion of the latter from "ordinary and necessary" expenses certainly does no violence to the statutory language. The general policy being clear it is not for us to say that the line was too strictly drawn.[2]

The two Supreme Court decisions most relevant to the present proceedings are *Textile Mills Corp.* v. *Commissioner, supra,* and *McDonald* v. *Cimmissioner,* 323 U.S. 57. In *Textile Mills* taxpayer, among other activities, acted on behalf of certain German textile companies to endeavor to obtain legislation providing for the return of German property seized during

[2] There does not appear to be any basis for taxpayers' contention (Br. 32-34) that "the theory of statutory re-enactment cannot be invoked" here because the regulation was not captioned under Section 23(a)(1)(A). As pointed out, *supra,* the Regulations repeatedly had been held applicable to Section 23(a)(1)(A). Furthermore, it is difficult to conceive that Congress was not aware of a regulation which for almost forty years prohibited the deduction for expenditures for, among other things, promotion or defeat of legislation and for campaign expenses.

World War I under the Trading with the Enemy Act. As brought out in the opinion of the Court of Appeals for the Third Circuit (117 F. 2d 62),[3] taxpayer employed a publicity firm to prepare news items, speeches, and editorial comment. It also employed an attorney, a former Congressman, to deal with members of Congress, and two attorneys, former government officials, to prepare a brochure setting out the legal questions involved in the wartime seizure of private property. At issue was the deductibility of the payments to the publicity firm and to the two latter attorneys. It did not appear that either the firm or these attorneys dealt directly with Congress. The expenditures were held nondeductible, the Court relying upon the regulation as prohibiting the deduction.

The *McDonald* decision denied the deductibility of campaign expenses incurred by a judge appointed to a vacancy who was running for election for a full term. The opinion of the Court (323 U.S. 57, 60, 62) refers to the principle of *New Colonial Co.* v. *Helvering,* 292 U.S. 435, that deductions are matters of legislative grace, and to "the disallowance of campaign expenses as consistently reflected by legislative history, court decision, Treasury practice and Treasury Regulations." Furthermore, the decision drew a distinction between the expenses "related to the discharge of his functions as a judge" which were deductible, and his campaign expenditures which "were not expenses incurred in being a judge but in trying to be a judge for the next ten years." It referred to "the explicit restrictions of § 23 confining deductible expenses solely

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[3] Taxpayer's statement in the present case (Br.44), that the Supreme Court reversed the Third Circuit in *Textile Mills,* is incorrect. Both Courts held the expenditures not to be deductible.

to outlays in the efforts or services—here the business of judging—from which the income flows." Finally, it stated that "To draw a distinction between outlays for re-election and those for election—to allow the former and disallow the latter—is unsupportable in reason." McDonald was unsuccessful in his campaign. *Mays* v. *Bowers, supra,* applied its reasoning to deny a deduction for expenses incurred in a successful campaign.

In *Sunset Scavenger Co.* v. *Commissioner, supra,* this Court denied a deduction for expenditures for pamphlets, newspaper advertisments, speakers, all of which were addressed to the public and were designed to avert the passage by the voters of a proposed ordinance which would have injured the business of garbage collection. The Court stated that the regulation prohibited the deduction. See also *Old Mission P. Cement Co.* v. *Commissioner, supra,* wherein this Court also denied a deduction for contributions to a fund to promote a state-wide referendum for an increased gasoline sales tax levy. The referendum was successful; road construction increased; and taxpayer shared in the increased sales of cement. Nevertheless, its expenditure was held to be for lobbying and therefore nondeductible.

In *Revere Racing Assn.* v. *Scanlon, supra,* taxpayer operated a greyhound race track under license, and expended sums for promotional advertising, public relations and legal fees to help persuade a majority of the voters of Suffolk County to vote to approve the continued licensing of dog races in that county. The First Circuit held that the sums expended were not ordinary and necessary expenses paid in carrying on any trade or business, i.e., the expenses of doing busi-

ness, but were to put the voters in a frame of mind that would give taxpayer a possible opportunity to do business later. Additionally, that court held that a deduction should be denied by Section 29.23(q)-1 of Treasury Regulations 111, which is identical here to Section 29.23(o)-1. "Although taxpayer's expenditures were made to influence voters rather than members of the legislation", the First Circuit held that such expenditures "come within the prohibition of the regulation," citing *Textile Mills.*

Contrary to the contention raised by taxpayers (Br. 42-58, 66-67, 74-75), the regulation is not limited to those expenditures which are improper, corrupt, or against "public policy", nor only to those where direct pressure is brought upon a legislature. Taxpayers would, in effect, narrowly construe each of the clauses of the regulation, limiting its application solely to lobbying; construing the term, lobbying, solely to appearances before a representative body; limiting the promotion or defeat of legislation to that enacted by a representative body; limiting the term propaganda to insidious propaganda; and limiting campaign expenses to those of running for office. Such a narrow construction is, as the District Court below held (R. 28-30), not supported by the regulation, by the relevant decisions or by the fundamental principles involved. Instead, the cases hold that the regulation prohibits a deduction for any of the listed items, regardless of whether the expenditure is considered to be against some conceived "public policy". Additionally, the cases hold that the regulation applies to an expenditure made to influence the voters, as well as to one made to influence legislators. Any other construction would be

senseless, particularly where, as here, the voters act as legislators.

The plain language of Section 29.23(o)-1 applies not only to deductions for expenses of lobbying, but it applies with equal force to amounts expended for the promotion or defeat of legislation, the exploitation of propaganda, including advertising other than trade advertising, and to contributions for campaign expenses. Furthermore, there is not any qualification in the regulation that only amounts which (Br. 42) "violate sharply defined national and state policies" should be disallowed. Instead, it appears that the regulation was not intended to differentiate between *good* or *evil* lobbying, *good* or *evil* propaganda, as is shown by its language which flatly prohibits a deduction for amounts expended for lobbying, for promoting or defeating legislation, or for the exploitation of propaganda. Additionally, the language of the regulation on its face, applies equally to expenditures to influence voters, as well as to members of a legislature.

Taxpayers rely (Br. 47-50) upon language in *Textile Mills* to support their contention that the Court there was prohibiting expenditures only for "contracts unenforceable on the ground of public policy" and only to amounts spent for "lobbying" before a legislature. However, it should be noted that the deductions which were disallowed related only to amounts expended for news items, speeches, editorial comment, and for a brochure setting out the legal questions involved in the wartime seizure of private property, and did not relate to the matters which the Supreme Court condemned as against public policy. Furthermore, it does not appear that the publicity firm or the two at-

torneys who prepared the brochure dealt directly with any legislature.

In *Sunset Scavenger Co.* v. *Commissioner, supra,* the advertisements, pamphlets, speakers, etc., for which the deduction was denied, were addressed to the public rather than to a legislature. Furthermore, it was not shown in that case that the expenses were contrary to any public policy. In *American Hardware & Eq. Co.* v. *Commissioner, supra,* p. 130, deductibility was denied to contributions to the National Tax Equality Association~~s~~, organized to conduct educational, scientific and research activities relative to disparities in federal and estate tax statutes and to disseminate information to civic organizations, the public, and the federal and state governments. The ultimate objective of its propaganda was revision of the tax structure, principally to eliminate special tax benefits for cooperatives. In answer to an attack in that case upon the applicability of the *Textile Mills* decision to items of expense which were not against "public policy", the Fourth Circuit held (p. 130) that it found no substance—

> in the additional objection that the decision in *Textile Mills Corp.* v. *Commissioner,* is limited to the non-deductibility of items which are against public policy or are morally wrong. Both of these objections are clearly untenable under that decision.

In *Roberts Dairy Co.* v. *Commissioner, supra,* p. 949, a contribution to the National Tax Equality Association was held nondeductible under the regulation although the association "did not engage in lobbying activities, had no congressmen on its mailing list and

lid not request to appear before congressional com-
nittees considering changes in tax statutes." In
Revere Racing Assn. v. *Scanlon, supra,* expenditures,
nade to influence the voters of Suffolk County to vote
avorably to permit the continued licensing of dog
aces, were clearly not against public policy. Further-
nore, these expenditures were made to influence the
oters and not a legislative body, which the First Cir-
uit held came (p. 819) "within the prohibition of the
egulation", citing *Textile Mills.* Thus, none of the
pplicable Court of Appeals decisions, have construed
he opinion in *Textile Mills* as narrowly as is contended
or by taxpayers, i.e., to limit the prohibition of the
Regulations only to those expenditures which are
against public policy or are made to influence a legis-
ature.

In the present case, it cannot be disputed that the
amounts here involved were expended for propaganda
o defeat legislation—to persuade the voters of the
State of Washington what should be the law as to the
etail sale of wine and beer.

Initially, the provisions of Initiative 13 had been
submitted to the state legislature. The legislature did
not act on this measure. Thereafter, in accordance
vith Article II, Section 1(a) and 41 of the Constitution
of the State of Washington, as amended by Amend-
nents 7 and 26, the proposal was submitted to the
voters of the state for approval or rejection. (R. 45-
46.) If Initiative 13 had been approved by the voters,
t would have become a law of the state and, subject
o some restrictions, would have been subject to amend-
nent or repeal thereafter by the state legislature.
Under such circumstances, by approving or rejecting
he Initiative, the voters were exercising legislative

powers with respect to substantive law of the stat *Senior Cit. L.* v. *Dept. Soc. Sec.,* 38 Wash. 2d 142, 15 228 P. 2d 478. Thus, where taxpayers expende amounts admittedly for propaganda to defeat Initiati 13 (R. 77, 79, 80-84, 112-116) these amounts we clearly expended to defeat legislation within the mea ing and intendment of the regulation.

The cases relied upon by taxpayers, such as *Co missioner* v. *Heininger,* 320 U.S. 467; *Lilly* v. *Commi sioner,* 343 U.S. 90; and *United States* v. *Rumely,* 3 U.S. 41, are not applicable herein. As the Supren Court points out in *Commissioner* v. *Heininger, supr* p. 470, and in *Lilly* v. *Commissioner, supra,* p. 9 while upholding the validity of the Regulations whi disallowed a deduction for lobbying expenses, the reg lation was not applicable to those cases.

Smith v. *Commissioner,* 3 T.C. 696 (Acquiescen 1944 Cum. Bull. 26), decided prior to *Textile Mill* held deductible contributions by a lawyer, in the beli it would help his practice, to the Missouri Institute f the Administration of Justice. The purpose was secure an amendment to the state constitution change the method of selecting certain judges. Th Tax Court emphasized (p. 702) that there was lobbying before the legislature itself, a ground f decision which lost its basis with the *Textile Mills* d cision, and is inconsistent with later decisions of th Tax Court. For example, in *McClintock-Trunkey C* v. *Commissioner, supra,* contributions, among other to the Washington Beer Wholesalers Association o posing the same proposed Initiative as is involved i the present case, were held nondeductible; in *Mosb Hotel Co.* v. *Commissioner, supra,* contributions t the Kansas Legal Control Council for an advertisin

ampaign looking to repeal of the prohibition laws ere held nondeductible; and in *Davis* v. *Commissioner, supra*, contributions to a liquor association to ersuade the voters to vote in a referendum to allow the etail sale of liquor were also denied a deduction.

CONCLUSION

For the reasons stated, the judgment of the District ourt is correct and should be affirmed.

Respectfully submitted,

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